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IN THE

Supreme Court of the United States

OCTOBER TERM, 1932.

Nos. 330 and 331.

PETER L. MCDONNELL, *Petitioner,*

vs.

THE UNITED STATES.

DOMINIC A. TRUDA, *Petitioner,*

vs.

THE UNITED STATES.

On Writ of Certiorari to the Court of Claims.

REPLY BRIEF FOR PETITIONERS.

The brief for the United States presents four points which this brief discusses. They are:

1. Taxing statutes containing provisions of limitation must be construed liberally in favor of the taxpayer, and not strictly construed in favor of the Government as contended in the Government's brief.

2. These taxpayers are not estopped to deny the validity of the waivers.

3. The cases are not controlled by *Aiken v. Burnet*, 282 U. S. 277; *Stange v. U. S.*, 282 U. S. 270; or *Burnet v. Chicago Railway Equipment Co.*, 282 U. S. 295.

4. The Revenue Act of 1926 does not give validity to the waivers here involved.

ARGUMENT.

I.

Taxing Statutes Containing Provisions of Limitation Must Be Construed Liberally in Favor of the Taxpayer.

The Government's brief at page 14 states:

> "Statutes limiting the rights of the Government must be strictly construed. Independent Coal & Coke Co. v. United States, 274 U. S. 640; Loewer Realty Co. v. Anderson, 31 F. (2d) 268, 269 (C. C. A. 2nd), certiorari denied, 280 U. S. 558."

The Independent Coal & Coke Co. case involves public lands and cannot possibly be construed as an authority in tax cases. In Loewer Realty Co. the Circuit Court of Appeals in dicta misstates the rule, as the Government has in its brief in this case.

In construing taxing acts this Court has consistently held that liberal construction in favor of the taxpayer applies to provisions of limitation as well as to other provisions.

In *Bowers, Collector of Internal Revenue v. New York & Albany Lighterage Co.*, 273 U. S. 346, 349, this Court, in construing Section 250(d) of the Revenue Act of 1921, a limitation statute against the government, said:

> "He [the collector] maintains that any ambiguity in the clause under consideration must be resolved in his favor. Undoubtedly the United States will not be held barred by a *general* statute of limitation unless, upon a strict construction in its favor, the United States and the claim sought to be enforced fairly may be held to be within the terms and purpose of the statute * * *. The limitation applies to petitioner [the collector] and to the claims. * * * The provision is a part of a taxing statute; *and such laws are to be interpreted liberally in favor* of the taxpayers (citing cases)." (Italics supplied.)

Later this same rule was reiterated in *U. S. v. Updike, et al.*, 281 U. S. 489, 496. The Court said:

> "In any event, we think this is the fair interpretation of the clause, and the one which must be accepted, especially in view of the rule which requires taxing acts, *including provisions of limitation embodied therein*, to be construed liberally in favor of the taxpayer. Bowers v. N. Y. and Albany Co., 273 U. S. 346, 349." (Italics supplied.)

In view of the foregoing it must be held that the law as announced by this Court is that the limitation provisions of taxing acts must be construed liberally in favor of the taxpayer.

II.

These Taxpayers Are Not Estopped to Deny the Validity of the Waivers.

Beginning at page 16 of the Government's brief, the argument is made that the taxpayers are estopped to deny the validity of the waivers on the theory that when they were filed the taxpayers "were seeking special relief under Section 210 of the Revenue Act of 1917 with respect to the partnership's income and profits taxes." That the taxpayers received no benefit and that the Government was not injured by the giving of the waivers is at once apparent.

Section 210 of the Revenue Act of 1917 provides:

> "That if the Secretary of the Treasury is unable in any case satisfactorily to determine the invested capital, the amount of the deduction shall be the sum of (1) an amount equal to the same proportion of the net income of the trade or business received during the taxable year as the proportion which the average deduction (determined in the same manner as provided in section two hundred and three, without including the $3,000 or $6,000 therein referred to) for the same calendar year of representative corporations, partner-

> ships, and individuals, engaged in a like or similar trade or business, bears to the total net income of the trade or business received by such corporations, partnerships, and individuals, plus (2) in the case of a domestic corporation $3,000, and in the case of a domestic partnership or a citizen or resident of the United States $6,000. * * *"

The record in these cases clearly shows (McDonnell R. 7, 8) that prior to the execution of the waivers here involved the Commissioner *had acted* under Section 210, *had determined* that invested capital could not be satisfactorily determined, and *had determined* that the partnership had been overassessed $75,141.86. As the Commissioner had made the only determination required by statute his sole remaining duty was to close the partnership case on that basis. Whether or not these taxpayers signed the waivers in their individual cases the fact would have remained that the partnership was entitled to special assessment and it had been so determined by the Commissioner.

The law is established that taxpayers do not have to exercise the initiative by "seeking" relief under Section 210 of the Revenue Act of 1917 as the Government contends was done by the instant petitioners (Government's brief p. 17) because the Commissioner acts of his own motion in those cases.

> "Under section 210 of the Act of 1917, as under section 327(a) of the Act of 1918, the Commissioner acts of his own motion whenever he is unable to satisfy himself that the valuation will be accurate if there is adherence to the statute." (*United States v. Factors & Finance Co.*, No. 141, decided by this Court January 9, 1933.)

The facts surrounding the giving of the waivers were as follows: On March 18, 1923, the Commissioner assessed against the partnership an additional tax of $100,005.14 which was protested; such protest was considered by the

Commissioner who, finding the case to be one within the purview of Section 210 of the Revenue Act of 1917, determined that the partnership had been overassessed in the amount of $75,141.86, and proposed the allowance of such overassessment and the consequent reduction in the amount of the assessment made March 18, 1923 (McDonnell R. 7). The Commissioner so advised petitioners and by letters addressed to them and the partnership, under date of November 30, 1925, December 17, 1925, and February 12, 1926, imposed upon them the necessity of executing the waivers here in question as a condition to his allowance of such overassessment (McDonnell R. 7, 8).

How an estoppel can be successfully invoked against petitioners in the face of these facts is quite beyond comprehension.

When the Commissioner determined that the partnership's case was within the purview of Section 210 and proposed that the additional tax theretofore assessed against it be reduced by $75,141.86, such action, we submit, terminated the Commissioner's discretion in the matter. Thenceforth his only course was to obey the mandate of the statute and forthwith reduce and abate such assessment against the partnership *pro tanto*.

Instead of complying with the law, however, the Commissioner *demanded* that petitioners execute the waivers in question *as a condition* to his compliance with the law. He demanded that petitioners do that which was *not* required of them by law, before he would do that which *was required* of him by law; before he would make them an allowance in respect of which he enjoyed no further discretion. He demanded that they give to him what purported to be a statutory right (the waivers) to collect that which *he admitted was uncollectible*, as a condition to his formal and official abatement of that tax which *he admitted had been erroneously assessed and was not legally collectible*.

Expressing it mildly, such action on the part of the Commissioner amounted to coercion and duress, for, as this

Court has held, legal duress exists where one is "* * * coerced to do the act in order to escape a greater evil" (*Maxwell v. Griswold,* 10 Howard 242, 256).

This Court has defined estoppel in *Dickerson v. Colgrove,* 100 U. S. 578, 580:

> "* * * The vital principle is that he who by his language or conduct leads another to do what he would not otherwise have done, shall not subject such person to loss or injury by disappointing the expectations upon which he acted. Such a change of position is sternly forbidden. It involves fraud and falsehood, and the law abhors both. * * *"

In the instant cases the element most essential to respondent's plea is lacking, *i. e.,* the Commissioner was not lead to do what he would not otherwise have done. The Commissioner, having determined that assessment should be under Section 210, had no alternative than to proceed under that section.

Here the petitioners neither made representations nor did they conceal material facts in order to induce the Commissioner to accept the waivers now under attack; they did not request the Commissioner to delay his collection of their individual taxes. On the contrary, they demurred for a period of three months to *his demand* that they execute the waivers and executed them at the end of that time (February 23, 1926) only in order to prevent the unjust and illegal threatened collection from the partnership of the $75,141.86 overassessment.

Still a further reason why estoppel does not exist in this case is the fact that when final action was taken in the partnership case the Commissioner was required by law (Sections 273 and 274, Revenue Act of 1926) to issue a notice of deficiency to the partnership with respect to the deficiency he sought to collect. This he did May 22, 1926 (McDonnell R. 9). The partnership, of course, had the right of appeal to the Board of Tax Appeals where the partner-

ship's case would have been adjudicated irrespective of any action on the part of the partners as individuals. The Board of Tax Appeals is empowered to pass on special assessment cases (see *Blair v. Oesterlein Machine Co.*, 275 U. S. 220).

It is submitted that respondent's plea of estoppel is not only untenable but is unconscionable and should not prevail.

III.

Case is Not Controlled by Aiken v. Burnet, 282 U. S. 277; Stange v. U. S., 282 U. S. 270; or Burnet v. Chicago Railway Equipment Co., 282 U. S. 295.

The Government in its brief argues that the three waiver cases mentioned in the headline control the cases at bar. It is obvious that such is not the fact as the three cases cited are easily distinguishable.

In the Aiken case the waiver was given before the enactment of any provision for waivers. The Court held (p. 281):

> "If authority was needed for the acceptance of such waivers, it may be found in the general broad administrative provisions of the respective Acts" citing the 1917 and 1918 Acts.

Beginning with the 1921 Act the taxing statutes have provided for the granting of waivers so the authority for waivers has since then been derived from the specific authority in the statute rather than from the general administrative provisions. "*Expressio unius est exclusio alterius.*"

The Stange case held that a waiver was valid even though executed after the expiration of the period of limitation. The waiver in the Stange case, however, was executed under the 1921 Act which contained no limitation on the assessment or collection of taxes barred prior to the enactment of the Act.

The Chicago Railway Equipment Co. case is not applicable because (p. 299):

> "In the case at bar, the assessment would not have been barred until June 16, 1924, five years from the date of the return, and after the enactment of the 1924 Act, so that §278(e) is wholly inapplicable."

IV.

The Revenue Act of 1926 Did Not Give Validity to the Waivers Here Involved.

The Government's brief states (p. 15):

> "All doubt as to the validity of the waiver under section 278 of the Revenue Act of 1924 is removed by section 278 of the Revenue Act of 1926."

because Section 278 of the 1926 Act provides that it shall not authorize assessment of a tax barred at the time of the enactment of the Act

> "unless prior to the enactment of this Act the Commissioner and the taxpayer agreed in writing thereto, * * *."

It is submitted that in the absence of more specific language than that used in the 1926 Act it must be presumed that Section 278 of that Act referred only to waivers which were legally effective when executed.

> "When it is claimed that a law is to have a retrospective operation, such must be clearly the intention, evidenced in the law and its purposes, or the court will presume that the lawmaking power is acting for the future only and not for the past; that it is enacting a rule of conduct which shall control the future rights and dealings of men, rather than review and affix new obligations to that which has been done in the past." (*White v. U. S.*, 191 U. S. 545, 552.)

See also *Shwab v. Doyle*, 258 U. S. 529, 534; *U. S. v. Magnolia Petroleum Co.*, 276 U. S. 160, 162; *Russell v. U. S.*, 278 U. S. 181, 187.

If the taxpayers' major premise is correct, that is, that the waivers were invalid when given, it must necessarily follow that when the 1926 Act was enacted the tax liability was barred. That meant that the liability was extinguished.

> "The bar of the statute of limitations against the United States in respect of any internal revenue tax shall not only operate to bar the remedy but shall extinguish the liability * * *." (Section 1106(a), Revenue Act of 1926.)

The taxes were collected while the 1926 Act was in effect (McDonnell R. 11, Truda R. 10). It is true that Section 612 of the Revenue Act of 1928 repealed Section 1106 of the 1926 Act as of the date of its enactment. On this point the Circuit Court of Appeals for the First Circuit in *Commissioner of Internal Revenue v. Northern Coal Co.* (No. 2716, decided January 3, 1933, and not yet reported) held:

> "The crux of this case, therefore, is the effect of Sec. 612 of the Act of 1928. While it repealed Sec. 1106 of the Act of 1926 as of February 26, 1926, did it thereby revive a tax liability which by Sec. 1106 had already been extinguished, and, if so, was the period for assessment extended by the waiver filed April 12, 1927?
>
> "The Board following its previous decisions, and what is understood to be the rule in the Circuit Court of Appeals, *Steiner Mfg. Co.*, 18 B. T. A. 740; *United States Refractories Corporation*, 23 B. T. A. 872; *Knight-Campbell Music Co.*, 23 B. T. A. 1234; *United States v. John Barth Company*, 27 Fed. (2d) 782; *Dobbins v. Commissioner*, 31 Fed. (2d) 935, held that the repeal of Sec. 1106 did not revive the liability and the waiver of April 12, 1927, was of no effect. Also see *Griffiths v. Commissioner*, 50 Fed. (2d) 782.
>
> * * * * * * * * *
>
> "In view, therefore, of the provisions of Secs. 607 and 609, and also of Sec. 322(c)(3) of the 1928 Act,

> and the apparent purpose of Congress in the recent Revenue Acts to speed up the determination of tax liability and the collection of taxes, we think the repeal of Sec. 1106 of the 1926 Act by Sec. 612 of the 1928 Act, following in order as it does the five preceding sections, which it is agreed were a substitute for Sec. 1106, did not and was not intended to revive a liability for the taxes of prior years, where they had been extinguished under Sec. 1106, nor to give validity to waivers filed after all liability for such taxes had been discharged,—since Congress plainly indicated by Sec. 506 of the same Act that it did not favor the continuation of the practice of filing waivers after the period of limitation had once expired, * * *"

In *Russell v. United States*, 278 U. S. 181, the identical argument was made as is made in this case. The Court states (p. 188):

> "The legislative history of the Act of 1924 lends support to the conclusion which we have reached. The changes introduced into the Act of 1926 cannot authorize construction of the earlier one not consonant with the language there employed."

It is submitted that the waivers in the instant cases must stand or fall pursuant to the provisions of the law in effect when they were executed, the 1924 Act, and cannot depend upon the 1926 Act for their validity.

In addition to the foregoing the orders granting certiorari in these cases were "limited to the question of the validity of the waiver under Sec. 278(c) of the Revenue Act of 1924." Because of this limitation there is no question before the Court with reference to the effect of the 1926 Act, and it cannot properly be discussed.

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January, 1933.